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IN THE

Supreme Court of the United States

OCTOBER TERM, 1968

No. 1122

THE FUND OF FUNDS, LTD.,
Petitioner,

—against—

ETHEL ROTH (suing as a stockholder in the name and in behalf of DREYFUS CORPORATION),
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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March 6, 1969

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Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

Petitioner, The Fund of Funds, Ltd., an open-end investment company with its principal office in Geneva, Switzerland ("FOF"), prays that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Second Circuit, entered in the above entitled case on December 6, 1968.

OPINIONS BELOW

The opinion of the United States District Court for the Southern District of New York (R. 134a-136a)[1] is

[1]References prefixed by "R." are to the printed Appendix of FOF in the Court of Appeals for the Second Circuit which is Volume 1 of the record certified by the Clerk of said Court.

reported at 279 F. Supp. 935 and also appears in Appendix A hereto. The opinion of the United States Court of Appeals for the Second Circuit, which is not yet reported, appears as Appendix B hereto.

JURISDICTION

The jurisdiction of this Court is invoked under 28 U. S. C. Section 1254(1). The judgment of the Court of Appeals was entered on December 6, 1968.

QUESTION PRESENTED

Section 30(b) of the Securities Exchange Act of 1934 (the "Act"), 15 U. S. C. Section 78 dd(b), provides that:

> "*The provisions of this title* or of any rule or regulation thereunder *shall not apply to any person insofar as he transacts a business in securities without the jurisdiction of the United States,* unless he transacts such business in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate to prevent the evasion of this title." (Emphasis supplied.)

The question presented herein is whether the above expressed Congressional policy, or national policy generally,[2] requires, or indeed permits, the application of the arbitrary "short swing" profits recovery provision of Section 16(b) of the Act [one of the "provisions of this title"] to transactions

[2]National policy in this context has been unequivocally recognized by both executive and legislative branches by the call by the President on January 1, 1968 for, among other things, "an intensified program to attract greater foreign investment in United States corporate securities, carrying out the principles of the Foreign Investors Tax Act of 1966."

initiated in Europe by a foreign-based and operating mutual fund [a person who "transacts a business in securities without the jurisdiction of the United States . . ."] where the Commission has not deemed it "necessary or appropriate" to prescribe, or even propose, any rules, merely because the transactions incidentally were conducted through the facilities or by the permission of the New York Stock Exchange?

STATUTES INVOLVED

Section 30 of the Act, 15 U. S. C. Section 78 dd, provides as follows:

> "FOREIGN SECURITIES EXCHANGES[3]
>
> (a) It shall be unlawful for any broker or dealer, directly or indirectly, to make use of the mails or of any means or instrumentality of interstate commerce for the purpose of effecting on an exchange not within or subject to the jurisdiction of the United States, any transaction in any security the issuer of which is a resident of, or is organized under the laws of, or has its principal place of business in, a place within or subject to the jurisdiction of the United States, in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors or to prevent the evasion of this title."

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[3]The Section caption, "Foreign Securities Exchanges," was drafted prior to the insertion of subsection (b) into Section 30, and, therefore, refers only to the subject matter of subsection (a). *See* Comment, *Extraterritorial Application of The Securities Exchange Act of 1934*, 69 COLUM. L. REV. 94, 106 (1969). Subsection (b) here at issue applies to a foreign "business in securities" generally and makes no reference to foreign exchanges.

"(b) *The provisions of this titie* or of any rule or regulation thereunder *shall not apply to any person insofar as he transacts a business in securities without the jurisdiction of the United States,* unless he transacts such business in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate to prevent the evasion of this title." (Emphasis supplied.)

Other pertinent statutory provisions are set forth in Appendix C hereto.

STATEMENT

The question of the extraterritorial applicability of the Act presented herein is before this Court for the first time and is of vital importance to the national interest of the United States in re-establishing and maintaining a favorable balance of payments,[4] to the foreign relations of the United States and to the maintenance of international respect for the administration of justice. At issue in this case is the applicability of the arbitrary "short swing" profit

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[4]It is no exaggeration to characterize the chronic balance of payments deficit problem as a matter of vital "international" as well as "national" interest. It has been described as "the chief threat to international monetary stability." BUS. WK., Feb. 22, 1969, p. 88.

Indeed, so vital is the problem and so crucial to its solution is increasing foreign investments in domestic securities that President Kennedy, on October 2, 1963, had appointed a Task Force directed, among other things, to review United States governmental activities which adversely affect foreign purchases of the securities of U. S. private companies. On April 27, 1964, this Task Force, headed by former Secretary of the Treasury Henry W. Fowler, issued its report to President Johnson, which emphasized the "special importance" of the "possible reduction or elimination of obstacles to the international flow of capital." REPORT TO THE PRESIDENT OF THE UNITED STATES FROM THE TASK FORCE ON PROMOTING INCREASED FOREIGN INVESTMENT IN UNITED STATES CORPORATE SECURITIES AND INCREASED FOREIGN FINANCING FOR UNITED STATES CORPORATIONS OPERATING ABROAD 36 (1964).

recovery provisions of Section 16(b) of the Act to foreign-based transactions by FOF, an open end investment company or mutual fund incorporated with nonresident status in Canada and having its principal place of business in Geneva, Switzerland, the result of which will be a windfall to the issuer which was a primary participant. The Court of Appeals below affirmed a District Court summary judgment for a sum certain against petitioner for an alleged violation of Section 16(b) of the Act under the circumstances hereinafter described.

FOF is one of the largest mutual funds in the world outside of the United States. From its base in Geneva, it transacts a business in securities of all types. At all times herein relevant, FOF's investment advisor was I. O. S. Management Company, Ltd., a Bahamas corporation ("Management Co."). Like FOF, Management Co. had its principal place of business in Geneva where it made investment decisions on behalf of FOF and implemented them by placing orders either with European offices of American brokers or directly with such brokers by means of overseas telephone or Telex. Neither FOF nor Management Co. maintained any place of business within the territorial jurisdiction of the United States (R. 57a-58a).

While FOF was the owner of more than 10% of the issued and outstanding Common Stock of Dreyfus Corporation ("Dreyfus"), it purchased Dreyfus Common Stock (R. 14a, 28a) listed on the New York Stock Exchange and, within six months after such purchases, ordered three sales in complete liquidation of FOF's holdings in Dreyfus (R. 16a-17a). The principal sale, aggregating approximately two-thirds of the total number of Dreyfus shares held by FOF, was made to Dreyfus itself in a special off-board transaction by permission of the New York Stock Exchange after negotiations in Europe between Management Co. and

a broker acting for Dreyfus (R. 60a, 109a, 113a).[5] Thus, the plaintiff in this derivative suit has achieved the anomaly of recovering a large sum of money in behalf of an issuer which was itself the purchaser in the principal transaction which allegedly violated Section 16(b).

The Dreyfus shares were originally purchased in nine transactions, six of which had been ordered by Management Co. through the offices of brokers in Europe and three of which had been ordered from Geneva through United States brokers by telephone or Telex (R. 15,-16a, 53a). The brokers in turn executed the purchases over the New York Stock Exchange. The sales, which were, in essence, private transactions, were consummated after the aforementioned negotiations held in Europe between Management Co. and representatives of a United States brokerage firm (R. 60a). For all that appears in the record, it may well be that negotiations were initiated by the American broker at the behest of Dreyfus.[6]

Management Co. received confirmations of the purchases in Switzerland and payments for the stock were made through the facilities of a Swiss bank acting through its American correspondent. With respect to sales, the stock was delivered in London against payment in Switzerland (R. 60a-61a). Thus, all profits were realized in Switzerland.

So far as FOF or Management Co. were concerned, it made no difference where or how the brokers chose to execute these transactions so long as the transfer was

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[5]The premature grant of summary judgment below closed the record before petitioner had an opportunity to probe whether Dreyfus was the sole purchaser.

[6]If so, and if the decision below is permitted to stand, the judiciary will have opened a lawful avenue to enable an issuer to ensnare a naturally unwary foreign investor into liability by inducing the foreign investor to sell the issuer's shares to the issuer at a profit which the issuer may then proceed to recover for itself.

effected. FOF would have been equally satisfied if the brokers had purchased and sold the shares in private transactions in Kuwait of Taipei instead of on the New York Stock Exchange. The sales by FOF to Dreyfus Corporation of Dreyfus Common Stock were conducted in a special off-board transaction by permission of the Exchange only because New York Stock Exchange Rule 394(a) requires Exchange permission for all transactions in listed securities conducted by its members off the Exchange. Here, of course, the brokers were member firms and since the stock sold by FOF was a listed security, compliance with Rule 394(a) was necessary. Otherwise, these private sales could easily have been consummated abroad without any contact with the Exchange since its marketing facilities were in no way necessary or utilized to enable FOF to sell.

On these facts, the District Court held the Section 30(b) exemption from the Act inapplicable by construing that Section as concerned only with transactions conducted on foreign securities exchanges and by determining that it had subject matter jurisdiction because New York was the situs of the "wrong" (R. 136a) (App. A., pp. 3a-4a). The Court of Appeals affirmed on the ground that, in its view, Section 30(b) did not exempt transactions involving, however incidentally, United States brokers and banks for such transactions were not "without the jurisdiction of the United States". (App. B, pp. 8a-9a.) Additionally, the court below doubted whether a foreign mutual fund such as FOF transacted "a business in securities" so as to qualify for the exemption (App. B, p. 9a), and stated that the effect of foreign transactions in violation of Section 16(b) of the Act was "as great as when the trader is an American" (App. A, p. 9a).

FOF contends, however, that the limitation by the court below of the Section 30(b) exemption to transactions

having no contact with our territorial jurisdiction renders it meaningless; that a mutual fund such as FOF, *per se,* transacts a "business in securities" and is, therefore, within the exemption; and that FOF's "short-swing" sales to Dreyfus, the true insider, had no jurisdictionally significant effect within the United States which justifies ignoring the usual presumption against extraterritorial application of the Act, much less the express congressional mandate of Section 30(b).

REASONS FOR GRANTING THE WRIT

This case presents a unique question of statutory interpretation which is vital to the United States' balance of payments and its international fiscal relations. FOF is one of many foreign institutions which invest foreign capital in the United States.[7] Through 1966, FOF alone had accounted for a half a billion dollars being pumped into the American economy from abroad (R. 62a); cumulatively, foreigners invested approximately $1,860,000 in 1968 in our securities market. N. Y. Times, Feb. 17, 1969, p. 4, col. 7. Congress has recognized the immense importance of attracting foreign capital[8] and, therefore, enacted the Foreign Investors' Tax Act of 1966, Pub. L. No. 89-809, 80

[7]In the 18 years prior to 1968, the United States ran 17 balance of payments deficits totalling $38 billion. In 1968, there was a slight surplus, but there would have been another substantial deficit were it not for almost $2 billion of United States securities bought by foreigners such as FOF. Bus. Wk., Feb. 22, 1969, p. 88.

[8]*See,* Metz, *Market Place: U. S. Idea, Fund for Europeans,* N. Y. Times, Jan. 9, 1969, p. 38, col. 7 (describing the off-shore investment funds); Malabre, Jr., *Cash from Abroad: Foreign Investments in U. S. Rise Sharply After a Long-Drought,* Wall Street Jnl., Oct. 14, 1968, p. 1, col. 6; *Dept. of Commerce Mounts Drive to help U. S. Businessmen Attract Capital Investments From Abroad,* Int'l Commerce, Feb. 5, 1968, p. 7; *Help for the Dollar,* Forbes, Feb. 15, 1968, p. 21; *Glamour Stocks Lure Foreigners,* Bus. Wk., Nov. 25, 1967, pp. 127-28.

Stat. 1539 (November 13, 1966). *See* U. So. CAL. 1968 TAX INST. 625 (1968).

Notwithstanding continuing Congressional efforts to encourage foreign investment and although Section 30(b) of the Act flatly exempts from its operation "any person insofar as he transacts a business in securities without the jurisdiction of the United States" in the absence of rules based on findings of necessity or propriety by the Securities and Exchange Commission (the "Commission"), the court below, *sua oponte,* sought to compensate for the total absence of such rules. It cavalierly substituted judicial for administrative rule-making by applying the harsh and arbitrary penal[9] sanctions of Section 16(b) to FOF. It is difficult to conceive of a greater *deterrent* to foreign investment in United States securities than to apply the many onerous strictures of the Act to foreign-based transactions in such securities, as would be required under the rationale of the court below.

FOF respectfully urges that not only is the application of the strictures of Section 16(b) to foreign investors under present circumstances inconsistent with well-established principles of international law, *see The 1964 Amendments to the Securities Exchange Act of 1934 and the Proposed Securities and Exchange Commission Rules—International Law Aspects,* 21 RECORD 240, 250 (1966), but significantly, that Congress had expressly delegated this delicate policy decision to the expertise of the administrative rule-makers to exercise their powers only after extensive public hearings and expert fact finding under the Administrative Procedure Act. Section 30(b) specifically authorizes the Commission, and *not the federal courts,* to prescribe "such rules and regulations" as it may deem necessary or

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[9]*See* 2 L. Loss, SECURITIES REGULATION 1087 (2d ed. 1961).

appropriate to narrow the exemption given, for good reason, to persons who transact a business in securities without the jurisdiction of the United States. Significantly, after almost thirty-five years of experience in administering the Act, the Commission has not deemed it "necessary or appropriate" to prescribe a *single rule* under Section 30(b).[10] This it not to suggest any rule-making reluctance on the part of the Commission. Indeed, it has exercised its rule-making authority under Section 16(b) no less than eleven times.

Furthermore, FOF submits that even if the Section 30(b) exemption be read so narrowly as to be inapplicable to the transactions herein, the Act must be given presumptively territorial application only, which presumption has not in any way been rebutted.

The importance of these issues to the future administration of the federal securities laws is particularly serious since the Second Circuit encompasses the nation's largest financial markets for foreign investors and the center of its securities industry. Moreover, the extraterritorial application of the Act is not a question appearing in but an isolated instance. Quite recently, the Court of Appeals for the Second Circuit had occasion, under circumstances materially different than those herein, to consider the role of Section 30(b) in limiting the reach of the Act in *Schoenbaum* v. *Firstbrook,* CCH FED. SEC. L. REP. ¶ 92,327, Dkt. No. 31408 (2d. Cir., Dec. 30, 1968), *rev'g in part on other grounds on rehearing en banc,* CCH FED. SEC. L. REP. ¶ 92,218, Dkt. No. 31408 (May 29, 1968), *aff'g on other grounds,* 268 F. Supp. 385 (S. D. N. Y. 1967). Unfortunately, the simplistic view of the problem taken by the court below in its *per curiam* opinion and the limited utility

[10]Nor did the Commission request any change in Section 30(b) in the extensive 1964 Amendments to the Securities Laws resulting from the massive *Special Study of Securities Markets,* H. R. Doc. No. 95, 88th Cong., 1st Sess. (1964).

of the brief discussion in *Schoenbaum* are grossly inadequate properly to rescue the lower courts from their obvious confusion concerning this vital issue. See, *e.g.*, in addition to the opinion of the District Court herein, *Kook* v. *Crang*, 182 F. Supp. 388 (S. D. N. Y. 1965); *Schoenbaum* v. *Firstbrook*, 268 F. Supp. 385 (S.D.N.Y. 1967), *aff'd on other grounds*. CCH FED. SEC. L. REP. ¶ 92,218, Dkt. No. 31408 (May 29, 1968), *rev'd in part on other grounds on rehearing en banc*, CCH FED. SEC. L. REP. ¶ 92,327, Dkt. No. 31408 (2d Cir., Dec. 30, 1968); *Ferriaoli* v. *Cantor*, CCH FED. SEC. L. REP. ¶ 91,615, 65 Civ. 1546 (S.D.N.Y. Dec. 28, 1965); *Ferriaoli* v. *Cantor*, 259 F. Supp. 842 (S.D.N.Y. 1966). See also *S. E. C.* v. *Gulf Intercontinental Finance Corp.*, 233 F. Supp. 987 (S.D. Fla. 1963), where the potential applicability of Section 30(b) was not even discussed. *See Generally* Comment, *Extraterritorial Application of the Securities Exchange Act of 1934*, 69 COLUM. L. REV. 94 (1969) (hereinafter referred to as *"Exchange Act Comment"*), the only known commentary on the subject.

Moreover, this issue is not one which is likely to disappear or ultimately be corrected in the course of decisions by various district courts and courts of appeal, from the most persuasive of which the "truth" may be expected to emerge. For all its importance to the American economy and foreign relations, this question is likely to arise primarily, if not only, in the courts of the Second Circuit, the senior court of which is demonstrably unwilling to grasp the complexity and gravity of the problem.

Still another compelling reason for this Court to grant the writ of certiorari sought herein is the necessity of inducing the Commission to accept its responsibility under Section 30(b) by promulgating rules thereunder, if it deems any to be necessary, after employment of proper administra-

tive procedure. The present language of Section 30(b) is clear and unequivocal that an exemption from all provisions of the Act is intended. The Congressional directive is equally clear that if the exemption is to be in any way limited, such limitation is to be imposed by the Commission, not the courts. The Commission has thus far abdicated its role to the courts which have fashioned simplistic *ad hoc* solutions to complex problems required to be solved only after full employment of the administrative process.

If the decision of the court below is permitted to stand, this inaction is all too likely to continue to frustrate the will of Congress. Under the narrow interpetation of Section 30(b) adopted below, the exemption has been so restricted as to be applicable essentially only when Congress could have had no legislative jurisdiction; thus, the Commission will have no occasion to exercise its rule-making power as directed by Congress.

For these reasons, as more fully developed below, it is essential that this Court exercise its supervisory power and grant the writ of certiorari sought herein.

A.

The Court of Appeals below has ignored the clear Congressional mandate of Section 30(b) and usurped the Commission's authority by rewriting the securities laws in the course of deciding cases brought by private parties. In view of the Section 30(b) exemption, the District Court had no subject matter jurisdiction over this case since that section provided an exemption from the entire Act, including Section 27 upon which the federal courts must rely for subject matter jurisdiction. The Supreme Court of the United States has the power and the duty to correct this error. *Louisville & Nashville R.R.* v. *Mottley,* 211 U. S. 149, 152 (1908).

The actions of the lower courts herein not only contravene the plain meaning of the statute; they are also jurisprudentially unsound in violating the well established principle of primary jurisdiction. The purpose underlying the concept of primary jurisdiction is essentially that the regulation of complex business problems is best accomplished, in the first instance, by administrative agencies "that are better equipped than courts by specialization, by insight gained through experience, and by more flexible procedure." *See Far East Conference* v. *United States,* 342 U. S. 570, 574-75 (1952), quoted in *United States* v. *Western Pac. R. Co.,* 352 U. S. 59, 64-65 (1956). This purpose is equally applicable to regulation under the federal securities laws where, as here, the resolution of a problem requires "a judgment which Congress has indicated is of the type for the Commission to make." *See S. E. C.* v. *Chenery Corp.,* 332 U. S. 194, 209 (1947).

In enacting Section 30(b) of the Act, Congress has clearly referred the decision as to the permissible scope of regulation of foreign investors to the Commission. Given our ever precarious balance of payments position which so heavily depends on foreign investments in American securities, *see* N. Y. Times, Feb. 17, 1969, p. 47, col. 7, and the international tensions generated by our judicial extraterritorial application of the Sherman Act, *see* Skiöld, *Antitrust Problems In International Trade,* 10 ANTITRUST BULL. 421, 445-48 (1965), Congress had good reason to entrust decisions as to extraterritorial enforcement of the securities laws to the sophistication and expertise of the administrative process. *Exchange Act Comment* at 97-99, 108 n. 76. As the product of administrative experience, appreciation of the complexities of the problem, realization of the statutory policies, and responsible inquiry into and treatment of material facts, the Commission's administrative

judgment is precisely what is required, at least in the first instance, for the effective resolution of an issue of the depth and importance as that presented herein, if the Congressionally intended exemption is to be narrowed. Unfortunately, as noted earlier, the court below has deprived the Commission of its proper function and substituted its own uninformed and restrictive view.

Thus, when Congress amended the Act in 1964, it assigned to the Commission the task of determining when foreign issuers should be exempted from otherwise applicable regulations. Section 12(g)(3) of the Act, 15 U. S. C. Section 78 l(g)(3). The history of the Commission's action under that mandate[11] demonstrates not only the wisdom of Congressional reliance on the administration process, *Exchange Act Comment* at 109-11, but, moreover, that Congress was, as recently as 1964, well aware of the need for administrative flexibility in regulating the foreign sector of the securities industry.

Yet, the court below undertook to determine that the Section 30(b) exemption did not apply to FOF's purchases and sales of securities on the New York Stock Exchange merely because brokers dealing with Management Co. had incidentally utilized certain facilities of interstate and foreign commerce. Thus, it was reasoned that FOF "was not transacting a 'business in securities *without the jurisdiction of the United States*'" (emphasis supplied). (App.

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[11]In addition, the history of the language employed in Section 12(g)(3) makes clear that Congress did not inadvertently promulgate the exemption in Section 30(b). *See* App. C, p. 11a. Indeed, as originally submitted by the Commission, the Section 12(g)(3) exemption was reversed. That is, securities of foreign issuers were to be exempt from Section 12(g) unless the Commission affirmatively acted—as it is required to act in Section 30(b)—to remove the exemption. For Section 12(g) purposes, however, Congress insisted upon its applicability to securities for foreign issuers unless the Commission acted to exempt. Clearly, Congress knows how to devise a conditional exemption if it so desires.

B., pp. 8a-9a.) This arbitrary construction of Section 30(b) is totally untenable unless it is assumed that Congress intended to enact a meaningless provision, *Exchange Act Comment* at 104-05, and is, furthermore. destructive to the beneficial end of continuing the substantial foreign investments in American securities, which end may well have been sought by Congress in enacting the exemption, *see Exchange Act Comment* at 108 n. 76.

The construction of Section 30(b) sought herein by FOF, as an affirmative exemption applicable to the transactions of foreign securities businesses in American securities markets, is confirmed by reference to both the apparent judicial prerequisite throughout the Act of the use of facilities of interstate or foreign commerce[12], and the reasonable premise that Congress did not intend, in promulgating Section 30(b), merely to utter excess verbiage. If Section 30(b) is to have any meaning at all, it must have been designed to exempt foreign based transactions in either (1) foreign securities; or (2) American securities, over (a) foreign exchanges and/or (b) American exchanges. Congress could not have realistically intended to exempt transactions of the first catagory simply because foreign investments in foreign securities would, even without such an exemption, be so devoid of contacts with the facilities of interstate or foreign commerce as to be beyond the legislative jurisdiction of Congress. *Exchange Act Comment* at 104-5. Similarly, as for transactions of the second category, those executed on foreign exchanges would commonly lack the requisite employment of the facilities of interstate or foreign commerce apparently deemed jurisdic-

[12]It should be noted that Section 30(a) prohibits a broker or dealer only from *utilizing the facilities of interstate commerce* to effect on foreign securities exchanges certain transactions to the extent deemed by the Commission to be contrary to the public interest.

tionally required[13] in Section 30(a) and, if they did involve such facilities, Section 30(a) rather than Section 30(b) would be applicable [at least to brokers or dealers, which by the broad definitions contained in Sections 3(a)(4), (5) and (6) of the Act, 15 U. S. C. Sections 78c(a) (4), (5) and (6), would include FOF and almost all other foreign securities businesses].

Although no constructive legislative history concerning Section 30(b) has been located, some indication that the construction suggested herein was that accepted by the Commission, and presumably Congress, appears from a careful review of the only specific commentary dealing with the extraterritorial application of the Act in the post-enactment period. In White, *Foreign Trading in American Stock Exchange Securities,* 49 J. POL. ECON., 655, 656-57, 698 (1940), it is reported that the Commission in 1937 had investigated complaints of manipulative practices by foreign investors on the New York Stock Exchange and had considered imposing restrictive measures. Although such measures were never imposed, that they were even considered is significant, for if all of the provisions of the Act were, as held by the court below, applicable to such foreign-based transactions on the New York Stock Exchange, it is unlikely that *special* measures would have been considered necessary.

Thus, if Section 30(b) is to have any substantive force, it must be interpreted as exempting transactions by foreign securities businesses in American securities over American exchanges unless and until the Commission observes the necessity for regulating such transactions and exercises its

[13]That such use of the facilities of interstate commerce was thought constitutionally necessary at the time of the enactment of the Act, see Brief of Thomas G. Concoran and Benjamin V. Cohen, *Hearings on H. R. 7852 and 8720 before House Committee on Interstate and Foreign Commerce,* 73rd Cong., 2d Sess., 926-32 (1934).

rule-making authority accordingly, which, of course, it has never done. Otherwise, almost every prominent European banking institution will find to its dismay that the interpretation of the court below has swept it under the jurisdiction of the Commission and the Act, since the typical European bank actively trades in securities listed on American exchanges both for its own account (and is thus a "dealer" by definition) and for the account of others (and is thus a "broker" by definition)[14].

It should be emphasized that FOF does not contest the *power* of Congress to make Section 16(b) of the Act applicable to its trading in United States listed securities, if domestic harm can be shown, under accepted jurisdictional principles of international law. Section 30(b), however, clearly demonstrates that Congress did not intend to *exercise* its power on any jurisdictional basis without the action of the Commission.

Unfortunately, the Second Circuit has emasculated Section 30(b) by holding FOF liable for acts performed abroad merely because of the incidental use of the facilities of interstate and foreign commerce by foreign and American brokers dealing with Management Co. In addition, the court below further nullified the intended exemption by doubting that FOF transacted a foreign "business in securities" so as to qualify for the Section 30(b) exemption. However, it is difficult to conceive of an organization more intimately engaged in the securities business than a mutual fund. Moreover, it is clear that if Congress had intended to exempt only banks, brokers, and dealers, but not mutual funds, it could have said so in precise language. Instead, Congress chose to exempt "any person" who conducts a

[14]The definitions of "broker" and "dealer" in Sections 3(a)(4) and 3(a)(5) of the Act exclude a "bank", but only a *domestic* bank, *see* Section 3(a)(6).

foreign securities business. As a mutual fund is obviously a corporate person which conducts a securities business, FOF is undoubtedly among the class of persons which Congress sought to exempt. *Exchange Act Comment,* at 107 n. 74.

B.

In any event, however, even if this Court should approve the narrow construction of Section 30(b) adopted below and render it meaningless, FOF submits that the Act, and Section 16(b) thereof, cannot reasonably be applied to the subject transactions of FOF under accepted principles of statutory construction and of international law. *See generally* RESTATEMENT (SECOND) OF FOREIGN RELATIONS LAW OF THE UNITED STATES, Sections 10(c), 17(a) and 18.

As Mr. Justice Holmes declared in *American Banana Co.* v. *United Fruit Co.,* 213 U. S. 347, 357 (1909), "all legislation is *prima facie* territorial." Thus, even if Congress had omitted Section 30(b) from the Act, this presumption of territoriality, as applied in 1934, would necessarily be read into the Act to provide a blanket exemption for foreign investors, *Exchange Act Comment at* 105, absent any indication of "detrimental effects" within the United States flowing from such foreign-based transactions which Congress could reasonably have intended to proscribe, *see Strassheim* v. *Daily,* 221 U. S. 280, 285 (1911).

Section 30(b), of course, specifically reinforces this presumption of territoriality. If the courts are to find this presumption rebutted, certainly they should do so only where a vital interest of the United States is affected in fact, not merely by hypothesis. *Compare American Banana Co.* v. *United Fruit Co., supra; Foley Bros.* v. *Filardo,* 336

U. S. 281 (1949); *Jackson* v. *S. S. Archimedes,* 275 U. S. 463 (1928), finding no such vital interest to be affected, *with Steele* v. *Bulova Watch Co.,* 344 U. S. 280 (1952); *United States* v. *Sisal Labs,* 274 U. S. 286 (1927); *Continental Ore Co.* v. *Union Carbide,* 370 U. S. 690 (1962); *Porter Co.* v. *Central Vermont Railroad Co.,* 366 U. S. 272 (1961), finding sufficient interest to warrant the exercise of jurisdiction. A technical[15] violation of Section 16(b) in which there is no harm to American investors (since, as here, the sale by the claimed insider was to the issuer and the alleged insider was not shown to have had any access to material inside information) simply is not a sufficiently grave offense[16] to war-

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[15]FOF was not present nor did it act within the territory of the United States. The determinative act of FOF herein, *i.e.,* Management Co.'s order of the sales within the six-month period, occurred entirely outside the United States. The incidental use by brokers dealing with Management Co. of the facilities of interstate and foreign commerce is, in itself, insufficient to justify the extraterritorial assertion of jurisdiction, inasmuch as such use was, so far as the record reveals, neither reasonably intended by FOF nor necessary to accomplish its purpose, *see* pp. 6-7, *supra. See* RESTATEMENT (SECOND) of FOREIGN RELATIONS LAW, *supra,* at Section 18 and *comment* f thereto.

[16]Although the Court below hypothesized that "the effect of this kind of trading [by foreign securities businesses] is quite as great as when the trader is an American" (App. B, p. 9a), it was unable, especially in the absence of any meaningful record (which was precluded by the improvident grant of summary judgment below), to support its conclusion by reference to either the Congressional findings underlying Section 16(b) or to any subsequent determination that transactions of foreign mutual funds owning in excess of 10% of a listed domestic security requires regulation for the protection of American investors. Presumably for this reason, Congress chose by enacting Section 30(b) to delegate such determinations to the Commission, and not to the federal courts. *See Exchange Act Comment* at 108.

Moreover, as FOF's sales were principally, if not entirely, to the issuer itself, Dreyfus, with respect to which FOF could not have been an "insider", FOF could hardly have profited by virtue of its position as a 10% beneficial owner.

rant the assertion of either the territorial or the protective principle, especially at the risk of defeating Congressional intention in Section 30(b) and, in any event, deterring important foreign investments in American securities. *See The 1964 Amendments to The Securities Exchange Act of 1934 and the Proposed Securities and Exchange Commission Rules—International Law Aspects,* 21 RECORD 240, 250 (1966). To the extent that FOF or other foreign investors may engage in practices deemed detrimental to domestic conditions, the protection afforded by Section 10(b) and Rule 10b-5, in conjunction with the Commission's rulemaking power under Section 30(b), is more than adequate.

FOF has not violated a rule that exists in the general law of civilized nations. It has not even committed what would have been a common law violation. It has merely infringed a harsh, arbitrary statute unique to the United States and widely disapproved abroad. See, Munter, *Section 16(b) of the Securities Exchange Act of 1934: An Alternative to "Burning Down the Barn In Order To Kill The Rats,* 52 CORN. L. Q. 69, 71 (1966). No hint has been given of any harm done to an American investor or financial institution. Since no adverse effect within the United States has been shown to have occurred, or even to have been reasonably likely, the presumption against extraterritoriality has not been rebutted.

CONCLUSION

In view of the mistreatment by the court below of the vital issue of the extraterritorial application of the Securities Exchange Act of 1934 in contravention of Section 30(b) thereof and the serious adverse impact on the national interest if the decision below is permitted to stand, it is

respectfully submitted that this petition for a writ of certiorari be granted.

Respectfully submitted,

ALLAN F. CONWILL
WILLKIE FARR & GALLAGHER
Attorneys for Petitioner,
The Fund of Funds, Ltd.
One Chase Manhattan Plaza
New York, New York 10005.

GILBERT SANDLER,
Of Counsel.

March 6, 1969

APPENDIX A

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF NEW YORK

ETHEL ROTH, suing as a stockholder in the name and in behalf of DREYFUS CORPORATION, *Plaintiff,* *—against—* THE FUND OF FUNDS, LTD., I. O. S., LTD. (S. A.) doing business as INVESTORS OVERSEAS SERVICES and DREYFUS CORPORATION, *Defendants*	67 Civ. 2027 # 34448

ATTORNEYS:

POLLACK GREENSPOON & SINGER, of New York, N. Y., for Plaintiff; DANIEL A. POLLACK, of New York, N. Y., of Counsel.

WILLKIE FARR & GALLAGHER, of New York, N. Y., for Defendants; VINCENT R. FITZPATRICK, KENNETH J. BIALKIN and GILBERT SANDLER, of New York, N. Y., of Counsel.

METZNER, *D. J.*:

This is a stockholder's derivative suit brought on behalf of Dreyfus Corporation, seeking recovery pursuant to §16(b) of the Securities Exchange Act of 1934, 15 U. S. C. §78p(b). Between September 15, 1966 and March 15, 1967, the defendant, The Fund of Funds, Ltd., owned in excess of 10% of the outstanding shares of the common stock of

Dreyfus. Within that six-month period, defendant bought and sold 33,200 shares of the stock, on which it realized a profit of $154,019.50. This suit seeks recovery of this profit. Plaintiff moves for summary judgment.

Defendant is a Canadian corporation with its principal place of business in Geneva, Switzerland. The orders for the purchase and sale of the stock were placed by telephone calls to brokers in New York City, who executed the orders on or through the facilities of the New York Stock Exchange. Payment for the purchase of the stock was made by a New York bank upon delivery to it of the certificates. The proceeds of the sale were deposited in a New York bank to the credit of a Swiss bank for the account of the defendant.

Defendant's first objection to the granting of this motion is that there are issues of fact regarding the purchase and sale of the securities, and as to the amount of damage. It is admitted that three of the nine purchase orders placed by the defendant were made by the president of the defendant by means of a telephone call from Geneva, Switzerland, to the broker in New York City. The president of defendant is supposed to have given the order for the other six purchases to a representative, in Switzerland, of a New York Broker, to execute the order. It is admitted that the New York broker, who in turn telephoned his office in presence of the defendant placed the order to sell the securities by means of a telephone call from Geneva, Switzerland, to the brokerage office in New York, but it is claimed that the negotiations leading up the placing of this order took place in Switzerland.

These contentions, either as to the six purchases or the sale, raise no issue of fact going to the determination of the controversy because the wrong complained of is that

an owner of more than 10% of Dreyfus stock made a profit on purchase and sale transactions in that stock within a six-month period. It is clear that all of the orders were intended by the defendant to be executed in New York. The purchase and sale took place on the New York Stock Exchange and that is the place of the wrong. *Gratz* v. *Claughton,* 187 F. 2d 46, 49 (2d Cir.), *cert. denied,* 341 U. S. 920 (1951). Consequently, it is immaterial what went on before the execution of the buy and sell orders.

A possible dispute as to the amount of damages cannot defeat this motion, since Fed. R. Civ. P. 56 provides: "A summary judgment, interlocutory in character, may be rendered on the issue of liability alone although there is a genuine issue as to the amount of damages." However, I find no genuine issue as to the amount of damages. A reading of the papers shows that the amount of damages claimed is the net difference between the purchase and sales prices. By this is meant that brokerage commissions and transfer taxes have already been taken into account. The affidavit in opposition states that defendant flatly denies that the amount claimed is the proper amount of damages, but it fails to set forth facts to substantiate this conclusion. See *Scolnick* v. *Lefkowitz,* 329 F. 2d 716 (2d Cir. 1964). Nowhere does defendant indicate any other expenses which should be taken into consideration.

Defendant finally contends that this court lacks subject matter jurisdiction. § 27 of the Securities Exchange Act, 15 U. S. C. § 78aa, provides that the district courts of the United States shall have exclusive jurisdiction of any action brought to enforce any liability created by the act. Defendant claims that § 30(b) exempts it from this grant of jurisdiction. The section provides that the act "shall not

apply to any person insofar as he transacts a business in securities without the jurisdiction of the United States. . . ." It is unnecessary for the court to determine whether this section refers only to brokers and dealers, or whether it applies to a mutual fund business operated by the defendant. The heading of the section refers to "foreign securities exchanges" and obviously refers to activities on such exchanges. The wrong here claimed occurred on the New York Stock Exchange, *Gratz* v. *Glaughton, supra*, and therefore this section does not limit the grant of jurisdiction contained in § 27. This case is stronger for sustaining subject matter jurisdiction than either *Ferraioli* v. *Cantor,* 259 F. Supp. 842 (S.D.N.Y. 1966), or *S.E.C.* v. *Gulf Intercontinental Finance Corp.,* 223 F. Supp. 987 (S. D. Fla. 1963). Neither of the cases dealt with a 16(b) violation. In both of them, it was necessary for the court to analyze the factual material to find the situs of the wrong in the United States.

The case of *Kook* v. *Crang,* 182 F. Supp. 388 (S.D.N.Y. 1960), relied on by the defendant, is not in point. That case dealt with a claimed violation of § 7(a) of the act, which covers the extension of credit by a broker-dealer. The court found that all the essentials of the transaction occurred in Canada, including the purchase of the securities which were held there as security for the credit that was extended. § 30(b) was found applicable because the word "jurisdiction" as used in the section "contemplates some necessary and substantial act within the United States." To the same effect is *Schoenbaum* v. *Firstbrook,* 268 F. Supp. 385, 394 (S.D.N.Y. 1967), a § 10(b) case where the court found that the fraud occurred in Canada in what was essentially a Canadian transaction. In the instant case, the wrong complained of occurred in the United States.

Motion granted. Settle order.

Dated: New York, N. Y.
February 8, 1968

CHARLES M. METZNER
U. S. D. J.

APPENDIX B

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

No. 27—September Term, 1968.

(Argued September 20, 1968 Decided December 6, 1968.)

Docket No. 32250

ETHEL ROTH, suing as a stockholder in the name and in behalf of Dreyfus Corporation,

Plaintiff-Appellee,

—against—

THE FUND OF FUNDS, LTD.,

Defendant-Appellant,

—and—

DREYFUS CORPORATION,

Defendant-Appellee,

—and—

I. O. S., LTD. (S. A.) doing business as Investors Overseas Services,

Defendant.

Before:

MOORE, FRIENDLY AND FEINBERG,

Circuit Judges.

Appendix B

Appeal from an order of the United States District Court for the Southern District of New York, Metzner, *Judge,* granting plaintiff's motion for summary judgment and directing judgment in favor of Dreyfus Corporation and against The Fund of Funds, Ltd., and from the judgment entered thereon.

ALLAN F. CONWILL, New York, N. Y. (Willkie Farr & Gallagher, New York, N. Y., and Vincent R. FitzPatrick and Gilbert Sandler, New York, N. Y. on the brief), *for defendant-appellant.*

DANIEL A. POLLACK, New York, N. Y. (Pollack Greenspoon & Singer, New York, N. Y.), *for plaintiff-appellee.*

PER CURIAM:

Plaintiff Ethel Roth, a stockholder of Dreyfus Corporation (Dreyfus), brought a stockholder derivative suit to recover short-swing "insider" profits made by The Fund of Funds, Ltd. (Fund), a Canadian corporation, on purchases and sales of common stock of Dreyfus on the New York Stock Exchange. The District Court granted her motion for summary judgment and directed judgment in favor of Dreyfus and against the Fund in the sum of $154,019.50 together with interest and costs. The Fund appeals.

The Fund, a mutual investment company and admittedly the beneficial owner of more than 10% of Dreyfus stock, made a profit on purchase and sale transactions within a

six-month period in violation of Section 16(b) of the Securities and Exchange Act of 1934 which provides that:

> . . . any profit realized by [the beneficial owner of more than 10% of the outstanding shares of the issuer] from any purchase and sale . . . of any equity securities of such issuer . . . within any period of less than six months . . . shall inure to and be recoverable by the issuer, irrespective of any intention on the part of such beneficial owner . . .
>
> 15 U. S. C. § 78p(b)

The Fund concedes, as it must, that it comes within this provision and that the net profit it received on such transactions would "inure to . . . the issuer." However, it seeks to bring itself within the exemption to this provision contained in Section 30 (b) of the Act.

That section, entitled *Foreign Securities Exchanges,* provides:

> The provisions of this chapter . . . shall not apply to any person insofar as he transacts a business in securities without the jurisdiction of the United States . . .
>
> 15 U. S. C. § 78dd

The Fund contends that it comes within the literal words of the exemption because, as a mutual fund, it "transacts a business in securities" and, as its offices are in Geneva, Switzerland, it transacts this business "without the jurisdiction of the United States." However, Section 30(b) is inapplicable because when the Fund bought and sold the securities in question on the New York Stock Exchange, utilizing New York City stock brokers to execute its orders

to buy and sell, and made payment for the purchases through a New York bank, it was not transacting a "business in securities without the jurisdiction of the United States." *Kook* v. *Crang,* 182 F. Supp. 388 (S. D. N. Y. 1960), heavily relied on by the Fund, dealt with a totally different situation where the transactions were effected outside the United States on the Toronto Stock Exchange. Moreover, it is more than doubtful whether "transacting a business in securities" can be read to cover the Fund's activities of investing in securities. *Schoenbaum* v. *Firstbrook,* —— F. 2d —, Slip Opinion 1968-Term, pages 2468-69 (2d Cir. 1968).

The Fund's further argument that, quite apart from § 30(b), § 16(b) should not be read to apply to transactions by foreigners in securities of American corporations, although carried out in the United States, ignores the fact that the effect of this kind of insider trading is quite as great as when the trader is an American. Congress had power to deal with such transactions and there is no reason for doubting its intention to include them within the sweep of § 16(b). See *United States* v. *Aluminum Co. of America,* 148 F. 2d 416, 443-44 (2d Cir. 1945).

Fund argues also that judgment should not have been granted insofar as its sales were to Dreyfus Corporation. However, the statute makes no exception where the transaction giving rise to the profit occurred at the incentive of the issuer, and we are not disposed to create one.

The Fund also asserts that the District Court erred in granting summary judgment because there were material issues of fact as yet unresolved. The only such issue as to which the Fund raises any substantial point is the net amount of profit realized from the challenged transaction.

However, this figure was uniquely within the knowledge of the Fund. The commission and any other proper deductions were known to the Fund and not to the plaintiff, and if the Court below relied on the amounts supplied by the defendant Fund, the Fund cannot attack that decision for its own failure to act.

The decision below is affirmed.

APPENDIX C

Section 12(g)(3) of the Securities Exchange Act of 1934, as amended, 15 U. S. C. § 781(g)(3), provides as follows:

> "The Commission may by rules or regulations or, on its own motion, after notice and opportunity for hearing, by order, exempt from this subsection any security of a foreign issuer, including any certificate of deposit for such a security, if the Commission finds that such exemption is in the public interest and is consistent with the protection of investors."

Section 16(b) of the Securities Exchange Act of 1934, 15 U. S. C. § 78p(b), provides in pertinent part, as follows:

> "For the purpose of preventing the unfair use of information which may have been obtained by such beneficial owner, director, or officer by reason of his relationship to the issuer, any profit realized by him from any purchase and sale, or any sale and purchase, of any equity of such issuer (other than an exempted security) within any period of less than six months . . . shall inure to and be recoverable by the issuer, irrespective of any intention on the part of such beneficial owner, director, or officer in entering into such transaction of holding the security purchased or of not repurchasing the security sold for a period exceeding six months."

Section 27 of the Securities Exchange Act of 1934, 15 U. S. C. § 78aa, provides, in pertinent part, as follows:

> "The district courts of the United States, the United States District Court for the District of

Columbia, and the United States courts of any Territory or other place subject to the jurisdiction of the United States shall have exclusive jurisdiction of violation of this title or the dules and regulations thereunder, and of all suits in equity and actions at law brought to enforce any liability or duty created by this title or the rules and regulations thereunder."